Exhibit No. ___ -THC (JYR-1THC)
Docket No. UT-050814
Witness: Jing Y. Roth
REDACTED VERSION

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Joint Application of VERIZON COMMUNICATIONS, INC. and MCI, INC. For Approval of Agreement and Plan of Merger	DOCKET NO. UT-050814

TESTIMONY OF

JING Y. ROTH

STAFF OF WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

September 9, 2005

REDACTED VERSION

Q. Please state your name and business address.

A. My name is Jing Y. Roth, and my business address is 1300 South Evergreen Park Drive Southwest, Olympia, Washington 98504-7250. My business e-mail address is jroth@wutc.wa.gov.

Q. By whom are you employed and in what capacity?

A. I am employed by the Washington Utilities and Transportation Commission (Commission) as an Industry Expert. My participation in this case is on behalf of the Commission's Staff (Staff).

Q. Have you prepared a statement of your qualifications?

A. Yes. A summary of my education and experience is provided as Exhibit No. ___ (JYR-2).

I. Purpose of Testimony and Summary

Q. What is the purpose of your testimony in this case?

A. On behalf of the Commission Staff, I will address the Application of Verizon Communications, Inc. (" Verizon") and MCI, Inc. ("MCI") for Approval of Agreement and Plan of Merger (" Joint Applicants").

I will make my recommendation to the Commission on whether the merger application should be approved, whether the approval is in public interest, and what necessary conditions should be imposed on the Joint Applicants.

Q. Have other Staff members filed testimony in the case?

A. Yes. Mr. Tom Wilson will present testimony providing an analysis of the current state of the market and data on competition for various services in Verizon's service territory in Washington (Exhibit No. ___-THC (TLW-1THC)). Ms. Kathy Folsom will present testimony to address the Joint Applicants' financial health and the predicted merger savings (Exhibit No. ___-THC (KMF-1THC)).

Q. Would you briefly summarize Staff's recommendation?

A. Yes. Staff recommends the Commission approve the proposed merger, but only with conditions that are necessary to mitigate the potential harm to competition in the post-merger environment and to provide merger benefits and savings to Washington consumers. As a condition of the merger, Verizon should be required:

1. to offer other competing carriers intrastate services at the same rates, terms, and conditions that Verizon offers to its affiliates, including MCI, by contract, interconnection agreement, or commercial agreement;
2. to provide service to unaffiliated competitive local exchange companies that is as good or better than the service levels it provides to its affiliates, including, MCI;
3. to offer Verizon local exchange customers who have chosen MCI as their long-distance carrier an opportunity to switch to an unaffiliated provider at no charge;
4. to resolve an outstanding dispute regarding the provision of basic local exchange service in an unserved area contiguous to Verizon's service area;
5. to make specific improvements to the local calling areas in three areas of the state;
6. to reduce its retail tariff rates for special access/private line services in Washington;
7. to cap its local service rates from July 1, 2007 to June 30, 2009; and

8. to guarantee that the retail service quality performance of both Verizon and MCI will not deteriorate after the merger.

Q. What is the purpose of imposing these conditions on the Commission's approval of the proposed merger?

A. Each of these conditions is intended to address elements of the transaction that would otherwise be harmful to the public interest. This merger is, broadly speaking, a transaction that has relatively modest benefits for the two companies and virtually no societal benefits. It does, however, have the potential to harm the public interest by reducing competition and customer choice in the areas where Verizon is the dominant provider of telecommunications services. These conditions will mitigate those harmful effects to the extent that, in Staff's assessment, the transaction can be found to be consistent with the public interest.

Q. Does the settlement in the rate case (Docket No. UT-040788) prevent the Commission in any way from implementing the conditions you have recommended?

A. No at all. Paragraph 40 of the Settlement Agreement for the rate case specifically states: "this Agreement does not affect the Commission's power on any issue in merger, sales or acquisition transactions that may require Commission approval."

Paragraph 50 of the **Narrative Supporting Settlement Agreement** (2/23/05) states:

> Merger. Another benefit for Verizon NW's customers is the inclusion of language in the settlement which clarifies that, in the event that the Commission undertakes a review of any Verizon merger, sale, or acquisition, this settlement does not limit the Commission's power to deal with any issue in the merger docket, including, for example, merger benefits for consumers.

II. Joint Petition for Approval of the Proposed Merger

Q. Could you describe briefly the request by the Applicants?

A. On May 27 the Applicants filed a Joint Petition requesting a declaratory order that the Washington Utilities and Transportation Commission (the "Commission") lacks jurisdiction under RCW Ch. 80.12 to investigate and approve the proposed transaction between Verizon and MCI. In the alternative, the Applicants seek expedited approval of the proposed transaction that will result in MCI becoming a wholly-owned subsidiary of Verizon.

Q. Would you please provide a brief description of the Applicants?

A. Verizon is a corporation with corporate headquarters in New York. The Company provides "telecommunications services on a regulated and unregulated basis in 29 states, Puerto Rico, and District of Columbia, serving 52 million access lines". (Joint Petition, Page 3.) Verizon Northwest Inc., Bell Atlantic Communications Inc. d/b/a Verizon long distance, Verizon Avenue Corp, and Verizon Select services Inc. are the Verizon subsidiaries registered to provide service in Washington (Organization Chart in Exhibit No. __ KMF-3). In Washington, Verizon offers local exchange telephone services to residential and business customers, intraLATA and interLATA toll services, access services, local private line, voice and data services, and Centrex. Verizon serves approximately 825,000 access lines in Washington and has annual intrastate operating revenue of $ 377 million.

MCI is a corporation with its headquarters in Ashburn, Virginia. MCI's subsidiaries that are registered in Washington to provide telecommunications services are MCI metro Access Transmission Services LLC; MCI WorldCom Communications, Inc.; MCI WorldCom Network services, Inc.; Teleconnect Long Distance Services and Systems Co. d/b/a/ Telecom USA; and TTI National, Inc. MCI offers services to residential, business, and enterprise customers ranging from local and long distance services to data, Internet, Sonet private line, and a whole range of high speed dedicated services.

Q. What do the Applicants state as to the operations in Washington after the merger is approved?

A. The Joint Petition, states: "after the transaction is completed, MCI will be a subsidiary of Verizon. MCI's regulated subsidiaries in Washington will remain as subsidiaries of MCI, LLC". (Petition Page 7). According to the Applicants, after the merger, there will be no change in the way the Commission regulates MCI and Verizon's regulated subsidiaries. Verizon and MCI will continue to meet all regulatory requirements.

III. Public Interest Standard and Merger Benefits

Q. Please explain your understanding of the public interest standard.

A. In order to approve the proposed merger, the Commission must determine that the transaction is consistent with the public interest. As with prior applications for approval of mergers, the Commission should review the proposal by examining the effect the merger will have on competition and market behavior, service availability and delivery, and service quality and reliability. The Commission should also examine the companies' claims regarding merger savings and real benefit to consumers. The Applicants state, through their Joint Petition and their Public Interest Statement, that the proposed transaction will not harm competition and that the merger will provide benefits to Washington consumers. These claims should be reviewed in light of the public interest standard set forth in WAC 480-143-170: "If, upon examination of an application and accompanying exhibits, or upon a hearing concerning the same, the Commission finds that the proposed transaction is not consistent with the public interest, it shall deny the application."

The Commission discussed the complexity of applying the public interest standard in a prior merger case (UT-991358 U S West, Inc. and Qwest Communications International, Inc.): "There is no bright line against which to measure whether a particular transaction meets the public interest standard. As we observed in another recent merger case, 'the approach for determining what is in the public interest varies with the form of the transaction and the attending circumstances.' [citing *In Re PacifiCorp and*

Scottish Power PLC, Docket No. UE-981627, Third Supplemental Order on Prehearing Conference (April 2, 1999), P 3.]"

Q. What is the financial benefit of the merger as stated by the Joint Applicants?

A. They state that the proposed merger will result in a net present value of approximately $7 billion in synergy benefits. (*Declaration of Stephen E. Smith,* FCC WC Docket No. 05-75, p. 1.) The merger is designed to create synergies by eliminating 7,000 jobs, reducing information technology costs, avoiding future costs for expanding out-of-region network, and achieving economy of scale for purchasing costs. (Id., p. 2.)

Q. Does Staff consider these estimated synergies to be a sufficient reason for approval of the merger?

A. No. While it is certainly true that it is better to have merger savings than not to have merger savings, the companies' claim of savings does not in and of itself represent a reason to approve the merger. Indeed, the level of synergies identified by the companies is actually quite small relative to the operations of the two companies. Together the companies had operating expenses of about $72 billion in 2004. If Verizon/MCI reduced their operating expenses by $700 million per year -- a reduction of less than 1 percent -- the net present value of those savings would be as great as the claimed synergies from this acquisition of MCI. Because there is so little in the way of efficiency gains from the proposed transaction, any harm to competition and customer choice will easily exceed the benefits. Verizon could achieve similar savings through modest expense reductions, but it is much harder to replace MCI as a source of pricing restraint on Verizon, Qwest, and the other incumbents.

Q. What do the Applicants claim concerning the effect of the merger on competition?

A. The Applicants claim that "[t]here will be no anti-competitive effect of this transaction in Washington or nationally because each company provides different market strengths." (Joint Petition p. 18.) They assert that the combination of their respective strengths will bring long-term benefits to consumers in this state.

Q. Does Staff agree with the Applicants' assessment of competitive impact?

A. No. MCI has for many years been an important competitor to the incumbent local and long-distance companies operating in Washington. The prospects for vigorous competition in the future would be strongest if MCI were to remain independent. As Mr. Wilson explains in his testimony, Verizon already dominates most of the markets in which it offers service, and the acquisition of MCI will increase its market power. These harmful effects can be mitigated, but it simply is not the case that the transaction has no harmful effect on competition.

Q. Has the Commission in past merger proceedings applied the public interest standard?

A. Yes. The Commission has done so in at least the two most recent telecommunications company mergers: U S West/Qwest Merger (UT-991358) and GTE/Bell Atlantic merger (Docket No. UT-991367). In both cases, the Commission approved the mergers by adopting settlement proposals that included conditions to protect the public interest and to share the merger savings with Washington consumers.

Q. Does Staff recommend that the Commission approve this merger with conditions?

A. Yes. Staff believes that the transaction can meet the public interest test if the Commission imposes eight conditions to ensure that competition will not be harmed, that consumers will be protected, and that some portion of the merger saving will flow through to Washington consumers. Later in my testimony, I will provide a detailed description and analysis of these conditions.

Q. Based on the Applicants' Petition and their Public Interest Statement, does the proposed merger meet the public interest standard by resulting in no harm to the public?

A. No. In the absence of Staff's proposed conditions, the merger would be harmful to the public interest. It could potentially harm competition and consumers. Verizon and MCI are both telecommunications providers in this state. The two entities are today competing in their respective service areas for long distance, special access service, and local services. MCI is also purchasing services and network elements from Verizon just like other CLECs in the state. Generally, competition brings benefits to customers in the form of choices, lower price, new products, and better service. The long-standing policy of this state for the telecommunications industry is to promote competition by creating a competitive environment with ease of entry for multiple suppliers of telecommunications services. This merger decreases the number of suppliers in certain segments of the market and runs counter to the public policy of promoting competition.

In summary, without the conditions recommended by Staff, the merger does not pass the public interest test, and Washington consumers will not see real benefits as claimed by the Applicants.

IV. Market Analysis and Conditions to Mitigate Competitive Harm

Q. Why is the analysis of the merger impact on competition in the relevant market necessary in this proceeding?

A. The impact of the merger on competition should be a critical factor in evaluating the proposed merger and determining whether the merger is in the public interest. Throughout the Petition and the Public Interest Statement, the Applicants state that the merger will not adversely affect competition in any market and they emphasize the availability of competitive alternatives. If there is a finding that the merger increases concentration in any of the markets that Staff has analyzed, specific remedies should be established by the Commission in order to offset the anticompetitive harm. The Commission should also consider the possibility of anticompetitive behavior after the merger and take steps to assure that the merger will not create new harm to competitors and that it will bring benefits to consumers.

Q. Has Staff provided market data and analysis?

A. Yes, Mr. Wilson has submitted testimony on this subject on behalf of Staff. Staff's market share analysis focuses on local exchange, in-state long distance, and special access/high capacity loop markets in order to determine if the merger will affect consumer choice and/or reduce the level of competition in these markets. Once Staff defines the relevant product and geographic markets, the Herfindahl-Hirschman Index ("HHI") is calculated to evaluate the impact of the merger on market concentration. (Wilson testimony at pp. 3-19; Exhibit Nos. ___ (TLW-4, 6, 8, 9HC).

Q. Please explain HHI.

A. The HHI is the most commonly used measure of market concentration. It is used as an aid in the interpretation of market data. The index, described in the Department of Justice's Horizontal Merger Guidelines is calculated by summing the squares of the individual market shares of all the participating firms in the relevant market. According to the guideline, an HHI under 1,000 indicates an unconcentrated market. An HHI between 1,000 and 1,800 indicates a moderately concentrated market. An HHI over 1,800 indicates a highly concentrated market. An HHI of 10,000 indicates a 100 percent pure monopoly market.

Q. What is the purpose of the HHI comparison?

A. While the HHI measures market concentration, the comparison of pre- and post-merger HHI is useful in determining the effect of the merger on the level of competition in the market. Staff analyzes any increase in the level of market concentration for matching conditions that will either prevent or mitigate the competitive harm.

Q. Should other factors be considered in evaluating the market and assessing the potential impact on competition?

A. Yes. An HHI should not be the only factor in evaluating the merger impact on competition in the market. Other criteria for review of the merger impact include ease of entry and access to the services that CLECs need to compete at fair, just, and reasonable rates, terms, and conditions..

Q. What is Staff's conclusion with regard to the impact of the merger on competition?

A. Based on the market data and analysis, Staff concludes that the overall effect of the proposed merger on competition will be negative for the businesses and households in the areas where Verizon is the incumbent local exchange provider. These negative effects on customer choice will be both direct and indirect. The direct harm is that customers will lose MCI as an alternative to the services offered by Verizon. The indirect harm is that other telecommunications companies that provide retail service using the wholesale or network services of other carriers will no longer have MCI has a supplier in competition with Verizon. In particular, Staff concludes that:

- The market for residential local exchange service is already very highly concentrated in the geographic areas where Verizon operates. Verizon's acquisition of MCI will eliminate its largest single competitor, but the effect on market concentration is negligible. The harm to competition is largely prospective, in that there will no longer be the possibility of greater competition from MCI.

- The market for business local exchange service is highly concentrated in the geographic areas where Verizon operates. Verizon's acquisition of MCI will increase concentration by a measurable amount. The increase in concentration would generally be unacceptable in an unregulated market and will likely prolong the need to regulate Verizon's business rates.

- The market for access/private line services is highly concentrated in the geographic areas where Verizon operates. Verizon's acquisition of MCI will increase concentration significantly -- an increase that would be unacceptable in an unregulated market and will likely prolong the need to regulate Verizon's access/private line services.

- Verizon's share of the residential long-distance market would increase significantly with the acquisition of MCI.

Q. How does Staff propose that the Commission mitigate these anti-competitive effects?

A. Staff recommends three conditions that will prevent possible anti-competitive behavior by the newly merged entity and will mitigate competitive harm in the post-merger environment. The conditions are:

1. Verizon should be required to offer other competing carriers the same rates, terms, and conditions for intrastate services that are made available to MCI and other affiliates.
2. The Commission should require Verizon to maintain parity for its wholesale performance measures between its own affiliate, MCI and other competing carriers.
3. Verizon should provide those customers who selected MCI as their long-distance carrier with an opportunity to change to another, unaffiliated carrier without incurring any service charge. Verizon should do this through a written notice to customers explaining the merger and providing a window of at least 60 days for making a change at no charge.

In addition, Staff is recommending that the Commission reduce Verizon's rates for intrastate special access services. This condition both mitigates the harm to competition and results in a sharing of merger benefits. I will discuss that condition later in my testimony when I discuss other conditions related to merger benefits.

Q. Why is it important for Verizon to offer other competing CLECs the same rates, terms, and conditions as it offers to MCI?

A. Since the 1996 Telecommunications Act, the existence of a certain balance of bargaining power between Verizon and MCI (together with AT&T) has played a important role in gaining access for the whole CLEC community to Verizon wholesale services and UNEs through interconnection agreement negotiations and arbitration proceedings. Although the impact in Washington state of the proposed Verizon/MCI merger on the telecommunications market is greater than the SBC/AT&T merger, the two mergers in combination create less bargaining power on the CLECs' side. Without AT&T and MCI to arbitrate new interconnection agreements, the CLECs remain vulnerable to costly and time-consuming arbitration of new agreements or amendments. The remaining CLECs in Washington simply will not have the matching resources to advocate against Verizon in arbitration and other regulatory proceedings necessary to establish rates, terms, and conditions for UNEs and other network elements that are no longer UNEs under Section 251 of the Telecommunications Act. The diminishing ability of small CLECs to negotiate and arbitrate interconnection agreements presents a barrier to entry.

Q. Should the Commission require Verizon to make the same rates, terms and conditions available to competitors with respect to its contracts and commercial agreements, just as it is required to do with respect to its interconnection agreements?

A. Yes. Verizon should be required to make the same rates, terms, and conditions available to other carriers that it makes available to MCI in contracts and commercial agreements as well. While it is important for the Commission to establish the condition that will extend the same treatment, rates, terms, and conditions for MCI, to other requesting carriers in the interconnection agreements, the Commission should also consider how CLECs will be able to continue to have access to certain UNEs that are not and will no longer be available as a result of the FCC's recent Triennial

Review Order (TRO) and its Triennial Review Remand Order (TRRO). Merely substituting Verizon's existing retail pricing for services that are functionally equivalent to these no-longer-required UNEs is insufficient. To mitigate this economic harm, the Commission should require Verizon to make available the same rates, terms and conditions in its contracts and/or commercial agreements with MCI to other requesting carriers.

Q. Why should the Commission require Verizon to guarantee parity between MCI and other CLECs for its wholesale service quality?

A. Verizon is already expected to provide its competitors with a level of service performance that is generally at parity with the level of service it provides to its own customers. Without these standards, there would be an incentive for Verizon to gain a competitive advantage by providing inferior service to competitors. The same incentive will exist with respect to MCI once it becomes a Verizon affiliate: Verizon could gain a competitive advantage by providing better service to MCI than it provides to unaffiliated competitors. Verizon today measures its service performance for many aspects of its service. Some of the standards, for example, are OSS Response Time, Order Confirmation Timeliness, Installation Quality, and Missed Repair

Commitments. It is vital after the merger for Verizon not to give favorable treatment to its new affiliate, MCI for these wholesale service performance standards; therefore, the Commission should require Verizon to guarantee that its wholesale service quality performance will be as good for other competing carriers as for MCI.

Q. What is the basis for the condition of no switching charge for long distance service?

A. The market analysis shows that the market share of Verizon's residential long distance service will increase significantly. Staff is concerned about less customer choice and such a dominant presence by Verizon in this market. These customers could have chosen Verizon as their long-distance provider and made the decision to use a competing provider. Their choice not to use Verizon will effectively be thwarted by this transaction. To address this concern, given that long distance services have been classified as competitive services, Staff proposes that the Commission requires Verizon to provide its customers who have selected MCI as their long-distance carrier with notice stating that there will be no switching charge if a customer wishes to switch long distance carrier within 60 days after the merger.

V. Flow through Merger Savings to Consumers

Q. Have the Joint Applicants filed testimony concerning the expected synergies from the merger?

A. No. While the public interest statement states that the savings will yield a net present value of $7 billion, (Public Interest Statement p. 15) the testimony filed on behalf of the Applicants does not discuss any specific saving amount for Washington.

Q. Has Staff estimated the merger savings that should flow through to Washington consumers?

A. Yes. Ms. Folsom has identified [redacted] in merger saving that should become an affirmative benefit to consumers.

Q. What are Staff's recommendations to ensure that savings are passed on to consumers and not just to shareholders?

A. Staff makes four recommendations:

1. Verizon should make an investment commitment to improve service in rural Washington. Specifically, Verizon should be required to extend service to certain unserved areas in Washington.
2. Verizon should upgrade its local service in certain areas by increasing local calling areas through rate center consolidation and by eliminating the flat and measured Premium Plus Adders.
3. Verizon should reduce its rates for intrastate special access services.
4. Verizon should be required to cap its local service rates at the level that was set by the Commission in its last rate case from July 1, 2007, to June 30, 2009.

Q. Please explain your first recommendation regarding unserved areas.

A. Over the years, Staff has been dealing with the issue of unserved areas where a few households reside with no basic landline telephone service. The unserved areas are, in many cases, adjacent to the service area of a local telephone company. The cost of serving the area and who should bear the cost is often controversial.

There is a complaint against Verizon by twelve residents on the Index-Galena Road currently pending before the Commission in Docket UT-050778.

Staff recommends that the Commission require Verizon to use a portion of its Washington jurisdictional merger savings to offer telephone service to the residents who live on the Index-Galena Road. While we are in an era of rapid technology development, promoting competition and consumer choice, we should not forget to achieve the fundamental goal of universal service.

Q. Please explain the condition for extended local calling areas.

A. Staff has identified three areas served by Verizon where it would be reasonable to improve the scope of the local calling area offered to customers. These changes benefit the local customers by enabling them to make local calls that today are charged as long-distance calls. In addition, the changes will benefit all customers in the state by allowing telephone number resources to be used more efficiently. The three changes are:

- Consolidate the three Skagit County rate centers – Anacortes, Mount Vernon, and SedroWoolley – into a single rate center. This will result in county-wide local calling for customers in Skagit County. Currently customers must pay toll charges to call between Anacortes and several communities north and east of Mount Vernon, including

Burlington. Consolidation of these rate centers also will allow for more efficient use of telephone prefixes and blocks by competing telecommunications companies.

- Consolidate the Arlington, Darrington, Granite Falls, and Marysville rate centers into a single rate center. By doing so, Verizon will improve the local calling range for some rural communities in Snohomish County and will allow for more efficient use of telephone prefixes and blocks by competing carriers.
- Eliminate the flat and measured Premium Plus Adders that currently apply to customers in Fairfield, Farmington, Latah, Oakesdale, Rockford, Rosalia, and Tekoa and to maintain existing unlimited usage service area for each exchange.

Q. What are special access services?

A. Special access service is a permanent, dedicated private-line type of connection between an individual subscriber and an interexchange carrier's point of presence.

Q. What is Staff's proposal to reduce Verizon's intrastate special access rates?

A. Staff recommends that Verizon's current rates for intrastate special access services be reduced to the level that is equal to Verizon's local interconnection rates for similar, if not identical functions. The Company's current interconnection rates and charges are contained in Verizon NW's Tariff WN U-21.

Staff's proposed average rates are shown in my confidential Exhibit No. ___C (JYR-3C). The net revenue impact is approximately negative [redacted]

Q. Why should the special access rates be reduced?

A. First, Verizon's special access rates exceed the costs that the Commission has previously determined in the generic cost docket. Staff's proposal of pricing these special access services at the level of its functional equivalent unbundled network elements (UNEs) moves the current retail rates closer to the costs of providing the services. Staff's proposal would also prevent rate arbitrage or "tariff shopping," because the underlying costs are the same for this type of service whether it is labeled as a "UNE" or as "special access."

Second, it is vital to reduce the retail rates for special access services today because CLECs rely on this type of service to compete with Verizon, and the FCC has eliminated high capacity and dark fiber transport and loops as required UNEs that are served out of ILECs' central offices that serve more than 24,000 business access lines or have three fiber-based collocators. Reducing Verizon's special access rates will mitigate the potential competitive harm of the merger when the high capacity loops will no longer be available as UNEs.

Third, in the settlement agreement approved by the Commission in Docket No. UT-040788, the special access rate reduction is discussed. It states:

> Nothing in this agreement shall preclude any Party from initiating, or requesting the Commission to initiate, or supporting any third party in a request for the Commission to initiate, or preclude the Commission from considering or resolving on the merits, any proceeding seeking to reduce or otherwise modify the intrastate special access rates that Verizon charges to competitive local exchange companies if Verizon significantly reduces or eliminates the availability of DS1 or DS3 loops or transport as unbundled network elements in its Washington service territory.

Because the TRRO has provided opportunities for Verizon to reduce the availability of the high capacity UNEs in Washington, it is likely that the issue of special access will come before the Commission if we do not provide an alternative such as special access lines at reasonable rates for CLECs to compete in the absence of high capacity loops.

Fourth, by establishing cost-based rates for special access services, the Commission will take a step necessary to encourage local exchange competition. The reduced rates should encourage facilities-based CLECs to purchase more intrastate high capacity services, and Washington consumers will benefit from effective competition.

Q. Please discuss in detail your third recommendation, which is to cap local rates for two years.

A. Staff recommends as a condition for the merger that the Commission require Verizon to cap its local service rates at the levels that are set in the settlement agreement in its last rate case from July 1, 2007, to June 30, 2009, a period of two years. During this period, Verizon could propose to reduce its local service rates and make other rate changes on a revenue neutral basis.

Q. Is there a specific dollar amount from the merger savings tied to this recommendation?

A. No, it is hard to calculate the revenue impact of this particular condition since there is no way to know when and if Verizon would otherwise propose rate increases for its basic local exchange services and file a rate case to request a revenue increase. This condition provides a benefit to consumers by giving them rate stability, but there is no specific cost to the company.

Q. Staff has identified [redacted] in merger saving for Washington consumers, is this conservative estimate?

A. Yes, Ms. Folsom in her testimony states that "Staff believes that its analysis is conservative given that the savings predicted on a national level for the years [redacted] were not quantified by the Companies at the Washington intrastate level and are likely to produce even greater savings."

The merger savings amount identified by Staff is at best an estimate for the immediate period of 4 years (2006 to 2009) after the transaction. In the long run, the merger benefit may result in greater synergy and generate revenue beyond the level that has been estimated today. Thus, the

Commission should require Verizon to implement merger conditions that will bring long term benefit to consumers.

VI. Verizon's and MCI's Retail Service Quality After the Merger

Q. Why should the issue of retail service quality be addressed in this merger proceeding?

A. In the first section of my testimony, I have discussed the merger application and the synergies as claimed by the Applicants. According to Applicants, the synergies are created by eliminating duplicative expenses and gaining operational efficiencies, and including an overall reduction of about 7,000 jobs. While synergies achieved from the merger may be a good outcome, consumers should be assured that the quality of telephone service provided by the merged companies will not deteriorate. It is important to discuss the issue of Verizon service quality, and to recommend that the Commission state its expectations of post merger retail service quality for Verizon in its order approving the merger application.

Q. Has the Commission considered retail service quality in a previous merger case?

A. Yes. The Commission believed it was imperative to monitor quality of service performance and network maintenance as a part of its consideration of the Bell Atlantic/GTE merger in 1999. The Commission issued an order approving and adopting a settlement agreement that set out additional commitments for GTE Northwest to improve its baseline level of consumer complaints, held orders, installation appointments, and trouble reports. The settlement also included a remedy plan if GTE failed to meet the standards.

Q. Which Commission rules regarding service quality are applicable?

A. Telecommunications companies are subject to the service quality reporting requirements in WAC 480-120-439; performance standards for installation or activation of service contained in WAC 480-120-105; response time standards contained in WAC 480-120-133; trouble report standards contained in WAC 480-120-438; network performance standards contained in WAC 480-120-401; and repair standards contained in WAC 480-120-440.

Q. Briefly describe the areas of service quality the Commission monitors for telecommunications companies.

A. The Commission generally monitors missed appointments, installation of basic service, trouble reports, trunk blocking, out-of-service interruptions or impairments, and complaints.

Q. What type of telecommunications companies does this rule apply to?

A. The current rule requires that Class A companies report the information required in WAC 480-120-439. Class B companies need not report as required in WAC 480-120-439(1). The classification of a company as Class A or Class B is determined by the percentage of state access lines – a company with two percent or more of the state access lines is a Class A company, and a company with less than two percent of the state access lines is a Class B. As of July 1, 2005, the two percent benchmark equates to approximately 76,500 access line.

Q. Did Staff review Verizon's service quality for this proceeding?

A. Yes. Staff reviewed Verizon's monthly service quality reports for the last six months. In that period, the Company was out of compliance with the rule only once – January. The violation was for an exchange that exceeded four trouble reports per 100 access lines for four months in a twelve-month period. Based on the information reported to the Commission by Verizon, the Company regularly meets the benchmark for trunk blocking. During the review period, there was only one month in which the Company fell below the benchmark standard.

Q. What does the Commission consider to be a service quality complaint?

A. A service quality complaint is a customer complaint related to the Commission's service quality standards. The Commission counts complaints related to quality of service, delayed service, and network congestion. In order to more fairly compare large and small reporting companies, the Commission calculates a percentage based on the number of service quality complaints per 10,000 access lines.

Although Verizon had 17 service quality-related complaints in the six months reviewed, Verizon's percentage was the second lowest percentage compared to the other four ILECs that the Commission monitors.

Q. What is your recommendation for Verizon retail service quality?

A. Service quality monitoring should be addressed by the Commission, as it did in its 1999 decision regarding the Bell Altantic/GTE merger. As a condition of the merger with MCI, the Commission should emphasize the importance of Verizon maintaining its service quality in order to ensure that the consumers will not receive a lower level of performance as a result of the merger. Staff is particularly concerned with the merger synergies that will be generated from cost cutting, work force reduction, and consolidations of operational centers. When viewed from a public interest perspective, although the public will benefit from greater efficiency, reduced costs, and increased innovation, it should not be done at the expense of the consumers who could experience deteriorating service quality as a result. Therefore, the Commission should require Verizon to guarantee its retail service quality performance will not deteriorate after the merger.

Q. What is the status of MCI in Washington?

A. MCI is registered as a CLEC in Washington. Since MCI is a Class B company it does not file service quality reports

Q. Has MCI supplied any information to indicate how it is performing in the state of Washington?

A. Yes. In MCI's Supplemental Response to Staff Data Request No.10, MCI submitted information based on the performance the ILEC delivered to MCI customers as reported by the ILEC. MCI submitted individual metrics from Qwest and Verizon.

MCI apparently is able to provide some of the information that is required by WAC 480-120-439 and related standard rules.

Q. Is the information consistent with Washington's service quality rules and reporting requirements?

A. Yes, for the most part. MCI submitted some information relevant to the metrics required by WAC 480-120-439, in other instances, the Company supplied only a portion of the requirement. MCI supplied the following:

1. the percentage out-of-service repairs cleared in 48 hours, but did not provide information on the percentage of impairments repaired in 72 hours;

2. the percentages of new or migration orders completed within five days, but did not include any information on the 90-day or 180-day requirement;
3. information pertaining to trouble reports, but supplied only a monthly percentage of the company as a whole, not by central office;
4. information on the percentage of repair commitments met and customer commitment orders completed, not the required missed appointment information; and
5. the information is based on orders or commitments *completed*, not based on orders *taken* as the rule requires.

Because MCI uses the facilities of the underlying ILEC, it is unable to provide information related to switching and trunking.

Q. Although the information supplied in the data request response may not be inclusive of the information required by the rule, how does MCI's service quality appear to be?

A. The percentage of installations *completed* in five days is considerably higher than the other CLECs that are currently required to file monthly service quality reports; in fact, the company is close to the 90 percent benchmark required for ILECs.

In general, MCI appears to be on track regarding trouble reports, as reported by the company as a whole; the Company is comparable to the other reporting companies regarding the repair of interruptions in 48 hours. For the six months reviewed by staff, MCI's complaints equaled 8.79 percent of the total number of tracked complaints of the reporting companies (and Verizon's complaints equaled 18.68 percent).

Q. Does this merger change the status of MCI from Class B to Class A company?

A. Yes. When and if the merger is approved, MCI is required by rule to file service quality reports with the Commission.

Q. Does this conclude your direct testimony?

A. Yes, it does.